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# *EFTA SURVEILLANCE AUTHORITY*

Doc. No. 97-1581-I  
Dec. No. 50/97/COL  
Ref. No. SAM 030.95013  
and SAM030.95019

## EFTA SURVEILLANCE AUTHORITY DECISION

OF 19 MARCH 1997

ON STATE AID TO DOCKING FACILITIES FOR SHIP REPAIRS  
IN THE HARBOUR OF AKUREYRI, ICELAND (ICELAND)

THE EFTA SURVEILLANCE AUTHORITY,

Having regard to the Agreement on the European Economic Area<sup>1</sup>, in particular to Articles 61 to 63 and 109,

Having regard to the Act referred to in point 1b of Annex XV to the EEA Agreement on aid to shipbuilding (Council Directive No. 90/684/EEC as amended by Council Directive No. 93/115/EC and Council Directive No. 94/73/EC)<sup>2</sup>,

Having regard to the Agreement between the EFTA States on the establishment of a Surveillance Authority and a Court of Justice<sup>3</sup>, in particular Article 1 of Protocol 3 thereof,

WHEREAS:

### I. FACTS

#### 1. Complaints and correspondence

By letter dated 31 August 1994, received and registered on 7 September 1994 (Doc. no. 94-13204-A), a complaint was lodged with the EFTA Surveillance Authority concerning alleged infringement of Articles 61 and 62 of the EEA Agreement. The complaint concerned certain support measures under the Icelandic Harbour Act No

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<sup>1</sup>Hereinafter referred to as the EEA Agreement

<sup>2</sup> These Council Directives, as adapted for the purpose of the EEA Agreement by the EEA Joint Committee Decisions No 21/95, 16/96 and 58/96 will hereinafter be referred to as the Shipbuilding Directive.

<sup>3</sup>Hereinafter referred to as the Surveillance and Court Agreement

23/1994, in particular regarding public support for investments in docking constructions for ship repairs (in Icelandic "Framkvæmdir á hafnarsvæðum við upptökumannvirki fyrir skip"), under Articles 24 to 26 of the Act.

However, at the time when the complaint was received the specific rules applicable within the European Community to State aid to the shipbuilding sector contained in the Seventh shipbuilding Directive (90/684/EEC) were not part of the EEA Agreement.

By Decision of the EEA Joint Committee No 21/95 of 5 April 1995 amending Annex XV (State aid) to the EEA Agreement the Shipbuilding Directive has been integrated into the EEA Agreement, with certain adaptations as laid down in the Decision. The Decision entered into force on 1 May 1995.

Following an enquiry by the EFTA Surveillance Authority after the Shipbuilding Directive entered into force in the EEA Agreement, the complainant has informed the Authority, that the circumstances, which gave rise to his complaint in August 1994, continued to prevail and that he would still request the Authority to examine the complaint.

By letter dated 24 October 1995 (Doc. no. 95-6144-D) the EFTA Surveillance Authority requested the Icelandic authorities to provide certain information on the matters raised by the complaint. By letter of 7 December 1995 the Icelandic Mission to the EU transmitted a letter from the Icelandic Ministry of Transport of 30 November 1995 containing a detailed response to the Authority's request for information.

By letter dated 16 October 1996 (Doc. no. 96-5779-D) the Surveillance Authority requested certain additional information, to which the Icelandic authorities responded by letter from the Icelandic Mission to the EU, transmitting a letter by the Ministry of Finance dated 9 December 1996.

By letter dated 30 November 1995, received and registered on 12 December 1995 (Doc. no. 95-7081-D), the Authority received another complaint on a related matter, i.e. concerning alleged State aid in the form of subsidised leasing by municipal harbour funds of docking constructions for ships, in favour of certain companies in the shipbuilding and shiprepair industry in Iceland.

The issues raised by the complaints have been discussed at meetings with the Icelandic authorities in Reykjavík on 3 March 1995 and 26 February 1996 as well as in numerous informal contacts.

## **2. Substance of the complaints**

### First complaint

This complaint concerns on the one hand certain provisions of the Harbour Act No 23/1994, which allow for State contributions to investments in docking constructions

for ships, and on the other hand alleged State aid in support of an investment in a floating dock by the Akureyri Harbour.

The complainant's State aid allegations concern the decision by the Akureyri Harbour to build a floating dock for ship repairs as well as the alleged decision of the Icelandic central authorities that the State Treasury will, on the basis of provisions in the Harbour Act, contribute up to 60% of the initial costs for building the dock and by the town of Akureyri, the port owner, to pay the remaining amount. The complainant claims that the purpose of this public investment was from the outset to lease the facilities to the shipyard Slippstöðin Oddi hf. in Akureyri.

The complainant furthermore alleges that when docking constructions are owned by municipal harbour funds<sup>4</sup> it is quite customary that they are leased to private companies at a rent which is far below the operating costs. According to the complainant the reason for this is that the local authorities concerned consider it important to maintain employment and therefore subsidise the operation. The complainant claims that such an aid arrangement distorts competition between private and public operators and considers it to be an essential prerequisite for such aid, if it is deemed to be necessary, that companies are equally eligible for it, regardless of their legal status.

### Second complaint

This complaint also refers to the Harbour Act and alleges that on occasions municipal harbour funds lease docking facilities at prices below costs and thus effectively subsidise certain enterprises, while others have to bear the full investment and maintenance costs of such facilities or pay full rental charges for their use.

The complainant then makes a comparison between on the one hand the terms and rental fee in the lease between the Akureyri Harbour and Slippstöðin Oddi hf. for the floating dock in Akureyri and on the other hand the terms and rental fee paid by Stálsmiðjan hf., a shipyard in Reykjavík, for a slipway facility leased from the Reykjavík Harbour. The complainant concludes that the terms of the former lease imply that the town of Akureyri is subsidising the shipyard Slippstöðin Oddi hf. and thus distorting competition to the detriment of competitors of Slippstöðin Oddi hf., both in Iceland and in other States parties to the EEA Agreement.

The current decision focuses on those parts of the two complaints, which relate to the investment project by the Akureyri Harbour. The provisions of the Harbour Act, which the complainants have also called into question, are examined in a separate decision.

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<sup>4</sup>Harbour funds are defined in the Harbour Act. According to part II of the act, harbours are owned by municipalities. A regulation shall be issued for each harbour, defining its boundaries and stipulating how the harbour is to be managed. Harbours are authorized to own stakes in companies operating in related activities. The Minister for Transport can decide by issuing a regulation to establish harbour co-operatives for the operation of harbours. Each harbour shall have a harbour fund to manage the finances of harbours and harbour co-operatives.

### **3. Submission by the Icelandic authorities**

The following gives a summarised account of relevant parts of the extensive reply by the Icelandic authorities to the Authority's request for information.

#### Decision to invest in the dock and provide public financing to the project

The preparations date back to 1992, when the national Lighthouse and Harbour Authority made a feasibility study for a dry dock in Akureyri. In addition to the need to cope with bigger and heavier ships, the existing slipway (from 1968) required frequent repairs and its foundations (esp. under sea level) had always been problematic. However, due to the estimated high costs the dry dock project was not realised, but the report by the Harbour Authority also pointed to the possibility of building a floating dock, which would be a considerably smaller investment.

In March 1993 the town council of Akureyri appointed a committee to study the possibility of a floating dock, and a report was delivered in March 1994. In April 1994 a committee appointed to carry out further preparations requested the confirmation of the Minister of Transport that the investment was eligible for support under the Harbour Act, to which the Minister replied in the affirmative by letter of 4 May 1994.

On 17 May 1994 the Akureyri Harbour and the town council decided on the following:

1. In principle, to purchase a floating dock with a capacity of 3.500 DWT;
2. To request the national Harbour Authority to prepare a tender and to design necessary installations;
3. To negotiate with the Ministry of Transport on the State's financing contribution to the project;
4. That improvements of the existing slipway be undertaken immediately following installation of the floating dock, so that it could carry 1000 DWT.

The tender for the purchase of the floating dock was announced on 26 June 1994.

In its letter to the EFTA Surveillance Authority of 30 November 1995 the Ministry of Transport states that to that date the investment had been financed exclusively by the Akureyri Harbour and that no payments had been made from the Treasury. The Akureyri Harbour had applied to the central authorities for a State grant to finance the investment, amounting to 40% of the costs (not 60% as alleged by the first complainant). Furthermore, no decision had yet been made by the Icelandic Parliament to award a grant to the project, but according to Art. 27 of the Harbour Act No. 23/1994, such grants require the approval of the Parliament. However, according to the letter by the Ministry of Finance of 9 December 1996, it was proposed to the Parliament (presumably in December 1995) to grant Akureyri Harbour the amount of ISK 128.8 million. The first instalment in the amount of ISK 31 million was included in the Treasury Budget for 1996, which was approved by Parliament on 22 December

1995. The remaining amount is expected to be provided for in the Treasury Budget for the years 1997-2000 without interest.

#### Initial business plan by the Akureyri Harbour

The preparatory report of March 1994, referred to above, contained the following initial business plan for the operation of the dock:

Estimated purchase price of dock:	135,0 MIKR
Installations	74,5 MIKR
Improvement of slipway	30,0 MIKR
Total initial investment costs	239,5 MIKR

Gross annual income was estimated between 11 - 16,5 MIKR, depending on capacity utilisation, and operating costs 9,3 - 10 MIKR. Hence, annual contribution to depreciation and capital costs was projected in the region 1,7 - 6,5 MIKR.

The Akureyri Harbour claims that the assumption when deciding on the investment was that rental income should cover the investment within a normal depreciation period.

According to the letter by the Ministry of Finance of 9 December 1996, the final investment costs for the floating dock and the related harbour construction, on the basis of which the government grant was decided, were the following:

<u>Purchase and installation of floating dock:</u>	
Purchase price of the floating dock	197.4 MIKR
Slipway	27.2 MIKR
<u>Harbour construction:</u>	
Embankment	11.7 MIKR
Harbour deepening	44.2 MIKR

The grant for the purchase and installation of the floating dock was determined to be 40% of the respective investment costs and 70% for the harbour construction. In amounts these grants are as follows:

Purchase of floating dock and slipway	89.7 MIKR
Harbour construction	39.1 MIKR

The Icelandic authorities note that embankments and harbour deepening are parts of the general harbour improvements which are financed by the harbours in Iceland for the general benefit of their users.

#### Lease with Slippstöðin Oddi hf.

A lease was concluded on 16 September 1995 between Akureyri Harbour (lessor) and the shipyard Slippstöðin Oddi hf (lessee). Besides the floating dock and the pertaining installations, the lease covers two slipways, for which there was an earlier lease with the same company, as well as non-exclusive use of a certain area of land where these facilities are located. The lessor undertakes to reconstruct within two years the foundations for the bigger slipway, in order that it can cope with 1000 DWT.

The lessee shall be responsible for and bear the cost of all regular maintenance of the leased property. He shall also pay insurance fees and all operating costs.

The rental fee for the dock and slipways is a fixed annual amount of 14 MIKR, starting from 1996 and paid quarterly, but for 1995 the fee is 1,75 MIKR, as the lease is effective only from 16 September 1995. The rent is fixed in nominal terms and is not directly linked to a price index. However, the rent shall be reviewed on 30 June 1997 at the latest, to take effect as from 1998, in the light of the final capital costs relating to the floating dock and its utilisation by the shipyard.

The letter by the Ministry of Finance of 9 December 1996 states that the rent was determined with a view to covering repayment of the investment costs incurred by Akureyri Harbour - i.e. the total investment costs less the anticipated grant from the State Treasury - over a repayment period of 25 years and assuming an annual interest rate of 7%. The basis amount for the investment costs used in this calculation was ISK 151.5 million.

The term of the lease is until 31 December 2005, unless the lessee prior to that date exercises the purchase option provided for in the lease. The lease is automatically extended for one year at a time, provided a written cancellation is not made by either party at 12 months notice. Slippstöðin Oddi hf. has priority over other interested parties for renewal of the lease.

The lease may only be cancelled due to important reasons, e.g. force majeure, non-compliance by either party, liquidity problems by the lessee or if either party is for other reasons unable to honour its commitments under the lease. In such circumstances the lease can be cancelled at three months notice.

If the lessee makes use of the purchase option the price shall be fixed, according to a formula specified in the lease, on the basis of the initial cost of the investment, indexed by the consumer price index from 1 September 1995, less the part of the already paid rent which reflects down-payment of the initial capital cost. The formula to be used for this purpose is reproduced in Annex I to this decision.

#### Other objectives and considerations

In their submission the Icelandic authorities indicate a number of objectives and considerations underlying in general the State's financing participation in investments in docking constructions for ships, as provided for under the Harbour Act, and in particular the decision by the Akureyri Harbour to invest in the floating dock.

It is stated that the objective of the Icelandic legislator in providing grants for docking constructions for ships is based on safety considerations and broad national economic interests, and that it is not devised to support the operation of individual companies in the shipbuilding industry.

As for the floating dock in Akureyri the main purpose of the public support to that project has been to ensure that there are adequate facilities to allow mandatory safety and maintenance work to be performed, besides regular ship repairs. The Icelandic authorities refer in particular to the fact that the size of ships in the Icelandic fleet has been increasing and that without the new investment there would be no docking facilities in the country with capacity to handle the bigger ships in the fleet. Hence, shiprepair services, which hitherto have been provided to the fleet at large, would no longer be available.

As a secondary objective the Icelandic authorities refer to the need to address the problem posed by a sharp downturn and severe structural difficulties experienced in recent years by the shipyard in Akureyri as well as by other Icelandic shipyards. These other considerations will be considered in more detail below.

## **II. APPRECIATION**

### **1. The presence of State aid**

The complainants have requested the Authority to examine whether the public involvement in the investment, financing and leasing of the floating dock in Akureyri constitutes a breach of Article 61 of the EEA Agreement. The Authority is therefore obliged to examine, firstly, whether State aid in the meaning of Article 61(1) of the Agreement was involved, and secondly, if so, whether the aid can nevertheless benefit from exemption under the relevant State aid rules.

Article 61(1) provides that "any aid granted by EC Member States, EFTA States or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Contracting Parties, be incompatible with the functioning of this Agreement".

It is beyond doubt that measures taken by central and municipal authorities to support an investment, which will be used for ship repairs - a mobile service in which considerable trade between Iceland and other Contracting Parties takes place - are measures taken through State resources, which are liable to affect trade between Contracting Parties.

The question whether certain undertakings or the production of certain goods are favoured must be considered in more detail. It must be kept in mind that on the one hand Article 125 of the EEA Agreement provides that the Agreement shall in no way prejudice the rules of the Contracting Parties governing the system of property

ownership, and on the other hand that according to Article 59, public undertakings shall be subject to the rules of the Agreement on competition, including those on State aid. On this basis the rules in Chapters 19 and 20 of the Authority's State Aid Guidelines<sup>5</sup> have been developed. By applying the test of the so-called "market economy investor principle", these rules clarify under which circumstances the financial relations between the State and public enterprises may be considered to involve State aid. According to this principle, State aid is considered to be involved when the State provides finance to a company in circumstances that would not be acceptable to an investor operating under normal market conditions.

The question of whether or not aid is involved in the present case is considered firstly at the level of the decision by the Akureyri Harbour and town Council of Akureyri to invest in the ship repair facilities, and secondly in the light of the lease which these authorities have concluded with Slippstöðin Oddi hf.

According to the initial business plan, on which the investment decision was to some extent based, total initial investment costs were estimated at 239,5 MIKR. Gross annual income was projected at 11 - 16,5 MIKR, depending on capacity utilisation. After deduction of operating costs, the net annual contribution to depreciation and capital costs was estimated at 1,7 - 6,5 MIKR. These figures imply a return on the investment which would be entirely inadequate from the point of view of an investor operating under normal market conditions. The fact that the authorities in Akureyri proceeded with the project in spite of the expected poor return on the investment is evidence that they have not acted as would be expected of a market economy investor.

However, it must be acknowledged that the above business plan was a preliminary one, and the Akureyri Harbour may at the time when it finally decided to go ahead with the investment have had more accurate and favourable estimates of its earnings on the investment. As it turned out the Akureyri Harbour decided not to operate the facilities itself, but to lease them to Slippstöðin Oddi hf., and by so doing has clearly secured better earnings on the investment than initially envisaged (net annual income (rent) of 14 MIKR as opposed to gross income of 11 - 16.5 MIKR). Under the circumstances it is considered appropriate to examine the matter from the point of view of possible benefits accruing to the end beneficiary, the shipyard, by assessing the terms of the lease with Slippstöðin Oddi hf.

It shall be noted that the selection of the lessee and fixing of the rental fee was not preceded by a tendering procedure. The terms of the lease must therefore be examined in the light of the market economy investor principle.

The Authority can accept the argument put forward by the Icelandic authorities that the relevant investment costs for the purpose of evaluating possible aid elements are those relating to the purchase and installation of the floating dock and rebuilding of the slipway, all of which is covered by the lease, and that the cost of other more

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<sup>5</sup>Procedural and Substantive Rules in the Field of State Aid. Guidelines on the application and interpretation of Articles 61 and 62 of the EEA Agreement and Article 1 of Protocol 3 to the Surveillance and Court Agreement. Initially adopted and issued by the EFTA Surveillance Authority on 19 January 1994 and published in the EEA Section of the Official Journal of the European Communities (No L231) and the EEA Supplement thereto (Nr. 32) on 3.9.1994.



general harbour construction, which was undertaken in connection with the project, is not relevant for this purpose. As the project had more or less been realised when the lease was made and the actual investment costs were then presumably known, it is considered relevant to rely on the figures for final investment costs provided in the letter by the Ministry of Finance of 9 December 1996, rather than the crude estimates made long before the lease was made. This implies that the relevant investment costs amount to a total of IKR 224,6 million. The annual rental fee, as from 1996, is 14 MIKR, under terms where the shipyard pays all operating and maintenance costs.

In Annex I calculations are made to determine the potential aid element in the lease. This is done by comparing on the one hand the initial cost of the relevant investments and on the other hand the sum of the present value of the income stream generated by the lease plus the present value of the estimated realisation (liquidation) value of the property at the end of the lease. The reference rate of interest for Iceland applicable in September 1995, as fixed by the Authority on the basis of point 27(3)(f) of the State Aid Guidelines, is used for discounting purposes. However, as the rent is fixed in nominal terms and not linked to a price index, the Authority cannot accept the suggestion by the Icelandic authorities to apply an interest rate of 7% p.a. (which corresponds to the reference rate of interest in real terms), but has instead used the reference rate of interest in nominal terms (for non-indexed loans) of 9,1%<sup>6</sup>. The provisions of the lease on the lessee's purchase option do on the other hand foresee that the price shall be linked to the consumer price index. When discounting the estimated realisation value of the property at the end of the lease, the Authority has consequently used the reference rate of interest in real terms, which at the time was 7,0% p.a.

As concerns the initial investment costs, it shall be noted that while it seems clear that when determining the rental fee in the lease the Akureyri authorities have only taken account of their share of the investment costs (i.e. they have deducted the anticipated State grant of 40%), it is for the present purposes relevant to base the calculation on the total investment costs, irrespective of how they are eventually split between the local and central authorities.

It shall also be noted that the realisation value of the facilities at the end of the lease is subject to a certain degree of uncertainty and alternative approaches of estimation are possible. The option chosen here is to use the formula provided in the lease itself, as a basis for the lessee's purchasing option<sup>7</sup>. On the above assumptions the result is that the lease involves an aid element of IKR 75,2 million (approx. ECU 0,9 million), which corresponds to 33,5% gross of the investment. After taking account of the prevailing level of corporate income tax in Iceland, the net (after tax) aid element is estimated at 22,4%.<sup>8</sup>

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<sup>6</sup> According to the lease, the rent shall be reviewed on 30 June 1997 at the latest, to take effect as from 1998, in the light of the final capital costs relating to the floating dock and its utilisation by the shipyard. However, no concrete information was submitted in response to the Authority's question on this review. It is therefore not possible to take account of this review clause.

<sup>7</sup> See Annex I for the details of this formula.

<sup>8</sup> For the sake of comparison, calculations have also been made assuming that the lease will continue unchanged for 25 years (the depreciation period which is assumed in the lease), in which case the margin of error due to the realisation or scrap value of the assets at the end of the lease is minimised.

## 2. Application of the relevant State aid rules

At the time when the investment decision was in principle made in May 1994 the rules applicable within the European Community on State aid to the shipbuilding sector were not part of the EEA Agreement. However, as argued above the presence of State aid in the current case, although also clear if examined on the basis of the investment decision, is established primarily by reference to the lease, which was concluded on 16 September 1995. At that time the Act referred to in point 1b of Annex XV to the EEA Agreement on aid to shipbuilding (Council Directive No. 90/684/EEC) had been integrated in the EEA Agreement with effect as from 1 May 1995.

The aid beneficiary is a company whose activity in the shipbuilding sector, including its ship repair activity of metal hulled sea-going vessels of not less than 100 GRT, is covered by the Shipbuilding Directive (cf. Article 1(c) of the act). Hence, the Shipbuilding Directive constitutes relevant rules for assessment in this case. As the aid has the character of regional investment aid and can at any rate not be accommodated under alternative rules on investment aid (i.e. rules on aid to SMEs), it must also be assessed under the rules on regional aid.

### Notification obligations

The Harbour Act No 23/1994 was enacted in March 1994 but not notified to the Authority, neither was the Authority informed of its predecessor, the Harbour Act No 69/1984, which apparently was in force at the entry into force of the EEA Agreement and also had provisions on state grants for docking constructions for ships<sup>9</sup>. It is recalled in this context that the Shipbuilding Directive did not enter into force within the EEA until 1 May 1995.

The lease with Slippstöðin Oddi hf., whose terms clearly reflect the expected state grant under the Harbour Act, was concluded in September 1995, after the Shipbuilding Directive had entered into force in the EEA Agreement. According to the letter by the Ministry of Transport of 30 November 1995, the Icelandic Parliament had by that time taken no decision to award a state grant to the project. However, according to the letter by the Ministry of Finance of 9 December 1996, it was proposed to the Parliament (presumably in December 1995) to grant the Akureyri Harbour the amount of IKR 128.8 million. The first instalment in the amount of ISK 31 million was included in the Treasury Budget for 1996, which was approved by the Parliament in December 1995. The remaining amount is expected to be provided for in the Treasury Budget for the years 1997-2000. Neither the lease between the Akureyri Harbour and Slippstöðin Oddi hf. nor the subsequent decision by the Icelandic Parliament in December 1995 were notified in advance to the EFTA

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The result is that the aid element in relation to the investment costs corresponds to 33,7% gross or 22,6% net.

<sup>9</sup>According to the Icelandic authorities, the Harbour Act enacted in 1994 involves the only change, as concerns the provisions on grants for docking constructions for ships, that the ceiling was raised from 40% to 60%.

Surveillance Authority before being put into effect. The Icelandic authorities have therefore failed to comply with the relevant notification requirements which are laid down in Article 1(3) of Protocol 3 to the Surveillance and Court Agreement, and in the case of aid to the shipbuilding sector also in Article 11 of the Shipbuilding Directive. The matter has consequently been dealt with by the Authority as a case of aid unlawful on procedural grounds, cf. Chapter 6 of the Authority's State Aid Guidelines. The Authority is nevertheless obliged to make a substantive assessment of the case.

### Regional aid rules

The beneficiary of the aid is located in the town of Akureyri, which according to the EFTA Surveillance Authority Decision No 103/96/COL of 28 August 1996 on the map of assisted areas for Iceland belongs to the area eligible for regional aid in Iceland, up to a ceiling of 17% net, plus a top-up of 10% gross for SMEs, if relevant.

In terms of full-time wage- and salary-earners the number of employees with Slippstöðin Oddi hf. was on average 114 in 1995. The company's turn-over in 1995 was ISK 596,3 million (approx. ECU 7.1 million), and its balance-sheet total at the end of that year was IKR 390.8 million (approx. ECU 4.7 million). No single shareholder or group of shareholders holds 25% or more of the capital or of the voting rights, except a holding company owning 37.4% of the shares, which the Authority understands does not exercise control over the company. These indicators imply that Slippstöðin Oddi hf. qualifies as an SME according to the definition set out in section 10.2 of the Authority's State Aid Guidelines. Hence, it qualifies for regional investment aid of 17% net plus the SME top-up of 10% gross, which combined corresponds to 23,7% net. Consequently, the estimated aid element of 22,4% NGE is within the relevant regional aid ceiling.

### Relevant provisions of the Shipbuilding directive

As regards investment aid to ship repair yards, Article 6(1) of the Shipbuilding Directive provides that such aid may not be granted unless it is linked to a restructuring plan which results in a reduction in the overall ship repair capacity in the EEA country concerned. In this context the EFTA Surveillance Authority may take into account capacity reductions carried out in the immediately preceding years.

Article 6(3) establishes that the amount and intensity of aid must be justified by the extent of the restructuring involved and that the aid must be limited to supporting expenditure directly related to the investment.

Article 6(4) states that when examining the aid, the Authority shall take account of the extent of the contribution of the investment programme concerned to such common objectives for the sector as innovation, specialization, working conditions, health, safety and the environment.

Slippstöðin hf. has for long been Iceland's biggest shipyard. In its heydays in the late 1970s and early 1980s, the company was engaged in newbuilding of fishing boats, smaller trawlers and cargo ships, in addition to conversions and repairs. At that time it had a workforce of 200 - 250. During the last decade or so the company as well as the shipbuilding sector in Iceland in general have, for a variety of reasons, experienced drastic reductions in output and market shares. Newbuilding of boats and ships has virtually ceased, and repair activities have also seen decline. Several companies have gone through liquidation or enforced financial restructuring, including Slippstöðin hf., whose finances were entirely rearranged and the company merged with the second biggest metal-working company in Akureyri, Oddi hf. According to the Icelandic authorities, the town of Akureyri, being at the time a major shareholder in Slippstöðin hf., together with the State Treasury, were closely involved in the restructuring of the company. Facilitating renewal of repair facilities has been regarded as an important element in a comprehensive restructuring plan. With reference to the above information, there is no reason to doubt that support to the project under consideration is linked to a restructuring plan for the shiprepair industry in Akureyri.

There are inherent difficulties in measuring the capacity of ship repair yards in physical terms. The approach taken here is the same as the EC Commission has relied upon in a few cases, to evaluate the capacity situation on the basis of employment or other general non-physical indicators.

The floating dock clearly implies an addition to the previous repair capacity of the yard. However, as foreseen in Article 6(1) the Authority may take into account capacity reductions carried out in the immediately preceding years. As outlined above there have been major reductions in output and employment in the company, from approx. 200-250 employees in the late 1970s and first half of the 1980s to approx. 100 in 1995, after Slippstöðin hf. and Oddi hf. had been merged to form Slippstöðin Oddi hf. At the same time there has also been a drastic decline in the industry as a whole (e.g. overall employment in the shipbuilding industry fell from an average of 977 employees in 1980-87 to 500 in 1994)<sup>10</sup>. Data is lacking on the precise division of employment between newbuilding, conversion and repairs. It is known that the collapse has been most pronounced in newbuilding, but repairs and conversions have also decreased considerably, esp. after 1989. This reduction is considered to outweigh the new capacity created by the floating dock as well as any possible productivity increases. Consequently, it is considered that when measured in terms of employment, the overall ship repair capacity in Iceland has decreased in recent years, in spite of the investment project at issue.

As to the question whether the proposed amount and intensity of the aid is proportional, it is firstly observed that the beneficiary of the aid, Slippstöðin Oddi hf., has for several years been in poor financial condition. However, there are now signs of improvement. The Icelandic authorities have demonstrated a clear need for upgrading of the docking facilities for ship repairs in Akureyri. There is good reason to consider that the achievement of the project under consideration will make an important contribution to the company's future viability and to safeguarding

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<sup>10</sup> Information based on a report by the Ministry of Industry from January 1995, "Árangur af jöfnunaraðstoð í skipasmíðaiðnaði árið 1994".

employment in Akureyri, where a contraction of manufacturing employment has taken place in recent years. For these reasons the amount and intensity of the aid is considered to be justified by the extent of the restructuring involved.

The presence of aid in this case derives from the fact that the Akureyri Harbour has in the lease with Slippstöðin Oddi hf. calculated the rent for the capital equipment on the basis of estimated initial investment costs net of the state grant, which it expected to obtain towards financing the investment. The aid granted is therefore considered to be limited to support only expenditure directly related to the investment.

Besides the above considerations, attention must also be paid to the reasons which prompted the Icelandic authorities to support the project.

The Icelandic authorities emphasise the vital importance of fishing and maritime transport for Iceland and the hazardous conditions in the seas round the country. Hence, it is necessary to provide safe harbours round the country, with adequate docking facilities, to allow mandatory inspection and necessary repairs and to ensure minimum disruption of the fishing operations, when repairs and service are needed. The Authority must duly acknowledge these objectives *inter alia* in the light of the provision in Art. 6(4) of the Shipbuilding Directive, which provides that the Authority shall take account of the extent of the contribution of the investment programme concerned to such common objectives for the sector as innovation, specialization, working conditions, health, safety and the environment.

The Akureyri Harbour submits that it has been necessary to ensure that the capacity of docking facilities matches the composition of the fleet at any given time. Due to a general increase in the size of ships, the existing facilities were already inadequate to allow docking of e.g. the biggest trawlers in the Iceland fleet, and no other yard in Iceland had such facilities. The purpose of the investment was therefore not to increase capacity, but to meet new requirements due to a general increase in the size of ships from the time the previous facilities were constructed and to secure a certain minimum degree of safety for the Icelandic maritime transport and fishing fleets by preventing that ship repair services, which hitherto had been provided, would no longer be available.

It shall finally be noted that according to Art. 6(2) of the Shipbuilding Directive the restrictions on capacity in Art. 6(1) shall not apply to the opening of a new shipyard in an EC Member State or an EFTA State which otherwise would have no shipbuilding facilities or to investments in a State's only existing yard, provided that the effect of the yard in question on the EEA market is minimal. Slippstöðin Oddi hf. is not Iceland's only shipyard. However, as submitted by the Icelandic authorities, the situation at the time was that without the floating dock in Akureyri, there would be no docking facilities in the country for the bigger vessels in the Icelandic fleet. In view of this, and given the vital importance for Iceland of efficient service to its fishing and maritime transport fleets, the underlying argument for the derogation in Art. 6(2) is considered to be relevant, although not necessary to rely upon in the present case.

For the above reasons the conditions set out in Article 6 of the Shipbuilding Directive are considered to be fulfilled. As concluded above, the aid also meets the general conditions for regional aid, as embodied in the map of assisted areas for Iceland.

### **3. Conclusions**

Assessment of the aid granted to the project under consideration has led to the following conclusions:

- The leasing by the Akureyri Harbour of the docking facilities for ship repairs - an investment made in anticipation of receiving a state grant under the Harbour Act - to the shipyard Slippstöðin Oddi hf. involves State aid to the shipyard estimated to amount to 22,4% NGE of the investment costs.
- As neither the Harbour Act, the investment project and the related State grant nor the lease with Slippstöðin Oddi hf. were notified to the Authority, the aid was granted in breach of the obligation to notify to the Authority in advance all new State aid.
- The level of the aid is within the relevant ceiling of the map of assisted areas for Iceland.
- The conditions for investment aid to ship repair yards set out in Article 6 of the Shipbuilding Directive are deemed to be fulfilled.

#### **HAS ADOPTED THIS DECISION:**

1. The EFTA Surveillance Authority has decided not to raise objections to the aid contained in the lease between the Akureyri Harbour and Slippstöðin Oddi hf. for a floating dock and other docking facilities for ship repairs, as belatedly informed of by the Icelandic authorities in the letter by the Ministry of Transport of 30 November 1995 and supplemented by the letter by the Ministry of Finance of 9 December 1996.
2. The Icelandic Government shall be informed by means of the letter at Annex II.
3. The complainants shall be informed by means of copies of the letter to the Icelandic Government.
4. The European Commission is informed in accordance with Protocol 27 (d) of the EEA Agreement by means of a copy of the letter to the Icelandic Government.

Done at Brussels, 19 March 1997

For the EFTA Surveillance Authority

Knut Almestad  
President

Hannes Hafstein  
College Member